March 14, 2005

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th St. and Constitution Avenue N.W.
Washington D.C. 20551

Re: Docket No. R-1217, Q31

Dear Ms. Johnson:

I am a third-year student at the William S. Boyd School of Law. Thank you for giving me the opportunity to participate in the Advanced Notice of Proposed Rulemaking ("ANPR") concerning the board's review of Regulation Z, set forth at 12 C.F.R. Part 236, which implements the Truth in Lending Act, 15 U.S.C. §1601(a). My comments will focus on item Q31 of the ANPR, which poses two questions:

1. Should Regulation Z be amended to require providers of open-ended credit accounts to disclose to consumers the financial cost of only making the minimum monthly payment on their account?
2. Should Regulation Z be amended to require providers of "quasi-open ended" footnote[1] credit accounts to disclose the total number of payments that would be needed to retire the debt if the customer only makes minimum payments when the account is opened?

1.Disclosing The Cost of Making Minimum Payments on Open-Ended Credit Accounts

It is well documented that providers of open-ended credit accounts set their "minimum payments" at levels far below the marginal cost of those payments footnote[2]. This is chiefly done for two reasons. First, it encourages consumers to keep a balance on their

footnote1 I use this term to describe credit accounts which are open-ended by their explicit terms but which are opened by a consumer to finance a particular item, such as a plasma television or a computer. (For example, Dell Computer offers "instant financing" to individuals ordering computers through their mall kiosks. Typically, these accounts are "branded" (if not explicitly controlled) by the merchant selling the item and the intent of both the buyer and seller is for the credit line to be devoted entirely to the specific purchase. They differ from more traditional forms of consumer-good financing because the merchant generally does not take a security interest in the item and because the "open-ended" terms of the account allows the merchant to maintain a continuing credit relationship with the customer after the initial item or items is/are paid off (in the hope that consumer will buy more from the merchant).

footnote2 Oren Bar-Gill, *Seduction by Plastic,* 98 N.W. U.L. REV 1373, 1408 (2004).

card, enabling the credit provider to earn income from interest charges footnote[3]. Second, since most Americans are notoriously bad at math footnote[4], they frequently fail to realize that only making a "minimum payment" may leave their balance over their credit limit when the payment is applied to their account. If this occurs, the credit provider is limited only by his or her own creativity (bounded by Regulation Z and, assuming they are a national bank, by the National Bank Act, 12 U.S.C. §85 (2005), and the Office of the Comptroller of the Currency or the FDIC) in determining what "penalty" fees to assess the hapless consumer[5].

In order to remedy this situation and to effectuate the spirit and intent of TILA, the board should require providers of open-ended credit accounts to print the following paragraph on every monthly statement they send, with the specific information that applies to each customer to be filled in where indicated.

> **NOTICE! As of {Closing date of statement} your balance is {$Balance}. If you made no further charges on this account after {closing date of statement} and you made only the minimum payment of {minimum payment}, you will pay off your account on or about {Month/Day/Year}. In addition, you would incur {interest charges} between {closing date of statement} and {payoff date}.**
>
> **[If applicable to the customer's account, include the next paragraph]**
>
> **Finally, making only the minimum payment of {minimum payment} will subject you to ${penalty fees} because your account will remain over its credit limit. You may be subject to additional fees if you fail to make your minimum payment on time.**

This disclosure has two main advantages. First, it explains to the customer in plain English what her prospective financial liabilities are. Second, by using **bold** print it imitates a transmission method credit card companies have used with great effect for years to get the attention of their customers when they're delinquent with a payment.

2. Disclosing the Cost of Making Minimum Payments on "Quasi Open-Ended" Credit

footnote 3 It also discourages what the industry prosaically refers to as "deadbeats", i.e. individuals who pay off their balance in full every month and (assuming their credit card carries no annual or other participation fees) have an interest-free loan from the credit provider. Indeed, assuming the card has affinity benefits such as "cash back from purchases" or frequent-flyer miles, the "deadbeat" customer is costing the credit provider money with every transaction she makes.

footnote 4 A recent survey ranked American high-school students (who are the credit users of tomorrow—or in some cases, are already the credit users of today) 24th out of the 29 member countries of the Organization of Economic Development (OECD). Michael Dobbs, "In a Global Test of Math Skills, U.S. Students Behind the Curve", WASHINGTON POST, Dec. 7, 2004, A01, Available at http://www.washingtonpost.com/wp-dyn/articles/A41278-2004Dec6.html (Last visited Feb. 15, 2005).

footnote 5 *See generally* Smiley v. Citibank (S.D.), N.A, 517 U.S. 735 (1996) (Court finds "late payment fees" are interest and governed by the National Bank Act rather than state usury and/or consumer protection statutes).

Since quasi open-ended credit providers operate in the same market as open-ended credit providers, they generally follow the same pricing structure described in 1., above. The decision of credit providers to price minimum payments below their marginal cost and the depressing state of American math skills referenced above apply with equal force to providers of quasi-open ended credit.

Indeed, given that the whole point of quasi open-ended credit is to facilitate the purchase of a consumer good in which the lender has no security and assuming the merchant isn't running the quasi open-ended credit operation as a loss-leader, the only avenues the merchant had to make money on the transaction is through interest charges and/or penalty fees. Finally, holders of quasi open-ended credit accounts typically make one large purchase, exhaust their account and proceed to paying it off, in contrast to users of true open-ended credit accounts, who are typically making payments and incurring charges at the same time.

This situation suggests the following mandatory disclosure language for quasi open-ended credit accounts:

> **NOTICE! As of {Closing date of statement} your balance is {$Balance}. If you made only the minimum payment of {minimum payment}, you will pay off your account on or about {Month/Day/Year}. In addition, you would incur {interest charges} between {closing date of statement} and {payoff date}.**
>
> **[If applicable to the customer's account, include the next paragraph]**
>
> **Finally, making only the minimum payment of {minimum payment} will subject you to ${penalty fees} because your account will remain over its credit limit. You may be subject to additional fees if you fail to make your minimum payment on time.**

Thank you for the opportunity to comment on this important issue. If you or the Board would like me to amplify or expand upon these comments I am happy to do so.

Sincerely,

Christina DiEdoardo